

CHILDREN'S HOSPITAL & RESEARCH
CENTER AT OAKLAND

INDEPENDENT AUDITOR'S REPORT
AND
CONSOLIDATED FINANCIAL STATEMENTS
WITH
SUPPLEMENTAL INFORMATION

DECEMBER 31, 2008 AND 2007

DATE RECEIVED:



AUDIT REVIEW #(s) 05170

Assigned To: Ryan

Date Reviewed: 8/28/09

Reviewer's Initials: GR

Date Review(s) Completed: 8/28/09

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Children's Hospital & Research Center at Oakland

We have audited the accompanying consolidated balance sheets of Children's Hospital & Research Center at Oakland (a California non-profit corporation) as of December 31, 2008 and 2007 and the related consolidated statements of operations and changes in net assets, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Children's Hospital & Research Center at Oakland's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Children's Hospital & Research Center at Oakland's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Children's Hospital & Research Center at Oakland at December 31, 2008 and 2007, and the consolidated results of its operations and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 28, 2009 on our consideration of Children's Hospital & Research Center at Oakland's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements of Children's Hospital & Research Center at Oakland, taken as a whole. The schedule of expenditures of federal awards and the schedule of expenses for County of Alameda grants are presented for purpose of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* and the County of Alameda, respectively and are not a required part of the basic consolidated financial statements. Such information has been subjected to the auditing procedures applied to the audit of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.



San Francisco, California
May 28, 2009

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATED BALANCE SHEETS
December 31, 2008 and 2007

	2008	2007
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 33,565,400	\$ 21,735,900
Investments	-	4,938,700
Assets limited as to use, held by trustee	7,383,700	20,906,000
Patient accounts receivable, net of allowance for doubtful accounts of \$7,970,400 for 2008 and \$6,688,700 for 2007	71,700,200	58,486,400
Grants and contract receivables	10,649,900	11,205,300
Other receivables	20,409,300	11,107,200
Supplies	3,535,400	3,328,000
Prepaid expenses	3,394,600	3,227,600
Total current assets	150,638,500	134,935,100
ASSETS LIMITED AS TO USE, HELD BY TRUSTEE, net of current portion	-	15,349,900
OTHER RECEIVABLES	19,687,000	25,723,500
PROPERTY, PLANT, AND EQUIPMENT, net	164,290,900	155,861,600
INVESTMENTS, net of current portion	156,023,200	182,899,500
OTHER ASSETS	2,044,900	2,084,000
Total assets	<u>\$ 492,684,500</u>	<u>\$ 516,853,600</u>

See accompanying notes.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN
UNRESTRICTED NET ASSETS
Years Ended December 31, 2008 and 2007

	2008	2007
UNRESTRICTED REVENUE, GAINS, AND OTHER SUPPORT		
Net patient service revenue	\$ 315,535,800	\$ 302,818,300
Other operating revenues	17,080,800	23,419,300
Net assets released from restrictions used for operations	60,020,100	50,423,300
Total unrestricted revenues, gains, and other support	392,636,700	376,660,900
EXPENSES		
Salaries and wages	164,218,100	152,191,300
Employee benefits	45,636,200	42,445,300
Supplies	38,260,200	35,737,200
Research and specific purpose grant expenses	55,310,100	49,886,600
Professional fees	42,049,800	37,173,600
Insurance and other direct expense	19,303,000	17,817,000
Depreciation and amortization	14,259,300	14,517,200
Purchased services	17,772,700	14,981,800
Provision for bad debts	12,463,500	11,337,300
Impairment of long-lived assets	7,843,600	-
Interest, net	4,392,900	3,954,600
Total expenses	421,509,400	380,041,900
Operating loss	(28,872,700)	(3,381,000)
NONOPERATING GAINS (LOSSES)		
Investment income	7,861,300	13,622,200
Change in fair value of basis swap	(41,600)	322,200
Loss on extinguishment of debt	-	(3,820,411)
Gain on extinguishment of swaps	-	2,663,831
Other	-	371,680
Total nonoperating gains (losses)	7,819,700	13,159,500
EXCESS OF REVENUE, GAINS, AND OTHER SUPPORT OVER EXPENSES	(21,053,000)	9,778,500
Change in net unrealized gains and (losses) on investments	(20,079,200)	(1,838,700)
Increase in pension liability (Note 6)	(35,555,200)	(22,260,800)
State and county grants for capital additions	4,129,200	-
Net assets released from restrictions for capital additions	637,200	5,821,700
Other	-	(472,200)
(Decrease) increase in unrestricted net assets	\$ (71,921,000)	\$ (8,971,500)

See accompanying notes.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2008 and 2007

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
(Decrease) increase in net assets	\$ (69,872,200)	\$ (12,115,700)
Adjustments to reconcile the increase in net assets to net cash provided by operating activities		
Depreciation and amortization	14,259,300	14,517,200
Provision for bad debts	12,463,500	11,337,300
Loss on extinguishment of debt	-	3,820,411
Net realized and unrealized gains and losses on investments	23,207,900	(3,320,686)
Donor restricted contributions	(18,600,200)	(4,720,100)
Change in fair value of basis swap	-	(2,975,845)
Impairment loss on long-lived assets	7,843,600	-
Changes in operating assets and liabilities		
Patient accounts receivable, net	(25,677,300)	(27,758,500)
Grants and contract receivables	555,400	(1,766,400)
Other receivables	(3,265,600)	(6,586,600)
Supplies	(207,400)	(446,000)
Prepaid expenses	(167,000)	(297,400)
Other assets	39,100	(3,594,896)
Accounts payable and accrued expenses	6,638,800	4,791,600
Accrued payroll and payroll related liabilities	805,300	6,186,500
Deferred revenue	676,500	2,328,200
Estimated third-party payor settlements	(70,600)	(444,800)
Accrued professional liability	165,500	458,700
Accrued workers' compensation liability	(6,473,200)	(1,871,910)
Liability for pension benefits	35,143,800	4,068,200
Other long-term liabilities	(1,183,000)	19,608,610
Net cash from (used in) operating activities	(23,717,800)	1,217,884
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property, plant, and equipment	(30,645,400)	(20,990,142)
Proceeds on sale of assets	113,200	3,728,727
Purchases of assets limited as to use	(4,629,900)	(147,720,437)
Sales of assets limited as to use	33,502,100	167,927,323
Purchases of investments	(174,305,900)	(6,638,300)
Sales of investments	182,913,000	10,853,800
Gain on basis swap	-	2,975,845
Net cash from investing activities	6,947,100	10,136,816
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from the issuance of debt	-	60,100,000
Proceeds from line of credit	10,000,000	-
Donor restricted contributions	18,600,200	4,720,100
Payments on long-term obligations	-	(71,751,000)
Net cash from (used in) financing activities	28,600,200	(6,930,900)
NET INCREASE IN CASH AND CASH EQUIVALENTS	11,829,500	4,423,800
CASH AND CASH EQUIVALENTS, beginning of year	21,735,900	17,312,100
CASH AND CASH EQUIVALENTS, end of year	\$ 33,565,400	\$ 21,735,900
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid for interest	\$ 4,783,662	\$ 2,852,500

See accompanying notes.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Temporarily restricted net assets: Net assets that are subject to donor-imposed stipulations that may or will be met either by actions of the Children's and/or through the passage of time. When a restriction is met, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of changes in net assets as net assets released from restrictions.

Permanently restricted net assets: Net assets subject to donor imposed stipulations that they be maintained by Children's in perpetuity.

Cash and cash equivalents - Cash and cash equivalents include certain investments in highly liquid debt instruments with original maturities of three months or less.

Investments - All investments in debt securities and short-term and long-term equity investments are measured at fair value in the balance sheet. Investment income or loss (including realized gains and losses on investments, interest, and dividends) is included the excess of revenues over expenses unless that income or loss is restricted by donor or law. Unrealized gains and losses on investments are excluded from the excess of revenues over expenses.

Life income trusts - At December 31, 2008 and 2007, CHRCF was remainderman for 222 life income trusts and charitable gift annuities (the "Trusts"), respectively. CHRCF was trustee for 21 of the 222 Trusts, and the assets of these Trusts are included in marketable securities and land, and in either temporarily restricted or permanently restricted net assets in the consolidated statements of financial position, depending on the donor restriction on the assets upon termination of the trust.

CHRCF, as trustee, is obligated to make annual payments to certain beneficiaries pursuant to irrevocable charitable remainder trust agreements. These trust agreements have various payment requirements, which include either fixed yearly payments or payments calculated at a required fixed percentage on the annual fair-market value of the trust's assets. A liability has been established for future payments under the outstanding unitrust and annuity contracts for which CHRCF is named as trustee. The liability is calculated using the most recent Internal Revenue Service mortality tables, with an interest rate assumption of 6% per annum. Upon the death of a beneficiary, CHRCF's interest in the trust becomes the unrestricted property of the CHRCF.

The remaining trusts for which CHRCF is not the trustee are recorded at the net present value of CHRCF's interest in the underlying trust assets, of which CHRCF will be the beneficiary, and are included in other receivables and temporarily restricted net assets in the consolidated balance sheets.

Assets limited as to use, held by trustee - Assets limited as to use primarily include assets held by trustees under bond indenture agreements and deposits required as security for Children's workers' compensation self-insurance arrangement. Amounts required to meet current liabilities of Children's and those limited use assets expected to be expended in the next twelve months are classified as current assets.

Supplies - Supplies are stated at cost, which is determined on the first-in, first-out method of accounting.

Property, plant, and equipment - Property, plant, and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable assets and is computed using the straight-line method. Leasehold improvements are amortized over the shorter of the life of the lease or the useful life of the improvements.

Gifts of long-lived assets, such as land, buildings, or equipment, are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service. Costs for maintenance and repairs are charged to expense as incurred. Estimated useful lives are as follow:

Land improvements	5 - 20 years
Buildings	10 - 35 years
Equipment	2 - 10 years

Deferred debt issuance costs - Costs associated with the issuance of debt are being amortized over the term of the related borrowing.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Contributions received may be designated by the donor for restricted purposes or may be without restriction as to their use. Contributions restricted by donors as to use or time period are recorded as temporarily restricted net assets until used in the manner designated or upon expiration of the time period. When there are no legally imposed restrictions on contributions or on income earned from restricted contributions, they are recorded as other unrestricted revenue when received.

Net patient service revenue - Children's has agreements with third-party payors that provide for payments to Children's at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per-diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Premium revenue - Children's has agreements with various Health Maintenance Organizations (the "HMOs") to provide medical services to subscribing participants. Under these arrangements, Children's receives monthly capitation payments based on the number of each HMO's participants, and recognizes as revenue during the period regardless of services actually performed by Children's. In addition, the HMOs make fee-for-service payments to Children's for certain covered services based upon discounted fee schedules. Premium revenues are included in net patient service revenues.

Charity care - Children's provides care to patients who meet certain criteria under its charity-care policy without charge or at amounts less than established rates for that service. Children's accepts all patients, regardless of their ability to pay. As Children's does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Charity care provided in 2008 and 2007, measured at established charge rates totaled approximately \$6,328,500 and \$5,900,200, respectively, for 1,141 and 1,684 patients, respectively. These charges are not included in net patient service revenues. Costs and expenses incurred in providing these services in 2008 and 2007, were approximately \$2,907,100 and \$2,711,200, respectively, and are included in Children's operating expenses.

Concentration of risk - Financial instruments potentially subjecting Children's to concentrations of credit risk consist primarily of bank demand deposits in excess of FDIC limits.

Children's grants credit without collateral to its patients, most of whom are insured under third-party payor agreements. Children's manages its collection risk by regularly reviewing its accounts and contracts and by providing appropriate allowances. The mix of receivables from patients and third-party payors is as follows:

	Years Ended December 31,	
	2008	2007
Managed care payors	46%	53%
Medi-Cal	8%	10%
California Children's Services	25%	18%
Medi-Cal managed care	10%	12%
Self-pay and other	11%	7%
	<u>100%</u>	<u>100%</u>

Income taxes - Children's is organized as a not-for-profit entity under the general nonprofit corporation laws of the State of California. Exemptions from federal income taxation under Internal Revenue Code Section 501(c)(3) and California franchise taxation have been obtained. Certain activities and subsidiaries may be subject to income taxes; however, such activities are not significant to the consolidated financial statements. Accordingly, no provision for income taxes has been provided in the accompanying consolidated financial statements.

Use of estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2 - NET PATIENT REVENUE

Children's has arrangements with third-party payors that provide for payments to Children's at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

Medi-Cal - Children's renders services to patients under a contractual arrangement with the Medi-Cal program, which includes patients that qualify for California Children's Services. Under the contractual arrangement, inpatient services are reimbursed on a per-diem basis, while outpatient services are reimbursed based on a schedule of maximum allowances. The net revenue from the Medi-Cal program was \$78,902,000 and \$80,263,000 for the years ended December 31, 2008 and 2007, respectively.

Children's contracts with the various Medi-Cal managed care plans in the State. In Alameda County the two programs are the local initiative and the mainstream plan. The local initiative is administered by the Alameda Alliance for Health (Alliance), while the mainstream plan is administered by Blue Cross. Both plans operate as state-licensed health maintenance organizations that provide health care services on a prepaid basis to enrolled Medi-Cal members residing in the county. Eligible members select the plan in which they wish to participate.

Children's established contractual arrangements with both of the plans. The effect of these arrangements was a shift from the previous fee-for-service reimbursement, under the original contractual arrangement with Medi-Cal, to an arrangement with the Alliance that provides reimbursement based on capitated lives, with separate case rate provisions for specific diagnoses. The Blue Cross plan provides reimbursement on a per-diem basis. Gross revenues, included in net patient service revenue, under each of these arrangements were as follows:

	2008	2007
Alliance - Capitation	\$ 24,093,600	\$ 20,844,000
Alliance - Case Rate	24,084,900	20,056,500
Blue Cross Medi-Cal	30,987,000	25,006,400

In addition to the reimbursement program discussed above, Children's received additional reimbursement from the State of California under the following programs:

Children's is a recipient of Medi-Cal funds under the various State of California programs, in particular The Private Hospital funds, disproportionate share funds (aka "DSH") and Supplemental Hospital funds. During 2008 and 2007, Children's recorded \$29,080,000 and \$36,595,000 in revenues related to funding from these programs. California Medical Assistance Commission negotiates the award amounts based on requests from eligible hospitals and the total pool of funding that is available for distribution at the time of the negotiations. This legislative funding is subject to retroactive reductions and potential future elimination.

For the years ended December 31, 2008 and 2007, Children's recorded \$7,331,900 and \$7,834,200, respectively, in revenues related to funding for Graduate Medical Education.

Laws and regulations governing the Medi-Cal and Medicare programs are complex and subject to interpretation. As a result, there is, at least, a reasonable possibility that recorded estimates will change by a material amount in the near term. Children's believes that it is in compliance with all applicable laws and regulations and is not aware of any significant pending or threatened investigations involving allegations of potential wrongdoing. While no such significant regulatory inquiries, other than discussed above, have been made, compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action, including fines, penalties, and exclusion from the Medicare and Medi-Cal programs.

Other - Children's also has entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment to Children's under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table shows the gross unrealized losses and fair value of the Children's investments as of December 31, 2008, that are not deemed to be other-than-temporarily impaired, aggregated by investment category. The fair market value of the investments declined primarily due to the general decline of the stock market related to the collapse of the housing market throughout 2008. All investments listed below have been in a continuous unrealized loss position for less than 12 months at December 31, 2008. There are no significant investments that have been in a loss position for more than 12 months.

	2008		
	Cost	Fair Value	Unrealized Loss
Marketable equity securities	\$ 34,000,173	\$ 29,468,100	\$ (4,532,073)
Corporate bonds	120,056,200	117,773,300	(2,282,900)
U.S. Treasury and Government obligations	426,500	426,500	-
Assets held in trust	9,838,286	8,355,300	(1,482,986)
	<u>\$ 164,321,159</u>	<u>\$ 156,023,200</u>	<u>\$ (8,297,959)</u>

Investment income, realized and unrealized gains (losses) consists of the following for the year ended December 31, 2008 and 2007:

	2008	2007
Interest and dividends	\$ 8,196,400	\$ 10,753,700
Realized gains on sales of securities	132,800	3,632,700
	<u>\$ 8,329,200</u>	<u>\$ 14,386,400</u>
Net unrealized losses on investments	<u>\$ (23,228,372)</u>	<u>\$ 1,844,700</u>

Effective January 1, 2008, the Children's adopted SFAS No. 157, *Fair Value Measurements*. SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 has been applied prospectively as of the beginning of the year.

SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS No. 157 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

- Level 1 Quoted prices in active markets for identical assets or liabilities
- Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in active markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities
- Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

Asset limited as to use, held by trustee - As quoted market prices are not available in an active market, the investments in money market funds are estimated by using pricing models and quoted prices of assets with similar characteristics; these investments are classified within Level 2 of the valuation hierarchy.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 4 - PROPERTY, PLANT, AND EQUIPMENT

Property, plant, and equipment consist of the following at December 31, 2008 and 2007:

	2008	2007
Land improvements	\$ 2,013,700	\$ 2,019,800
Buildings	216,343,000	206,989,600
Equipment	88,239,100	77,471,900
	306,595,800	286,481,300
Allowances for depreciation	(162,353,100)	(148,815,900)
	144,242,700	137,665,400
Construction-in-progress	11,379,500	9,527,500
Land	8,668,700	8,668,700
	<u>\$ 164,290,900</u>	<u>\$ 155,861,600</u>

The cost to complete the construction-in-progress at December 31, 2008 is estimated to be \$421,504,000. Depreciation expense totaled \$14,162,200 and \$14,451,600 for the periods ended December 31, 2008 and 2007, respectively. Additionally, depreciation expense of \$1,778,100 and \$1,652,300 for the periods ended December 31, 2008 and 2007, respectively, related to research specific property, plant and equipment.

During the year management changed the plans for the construction of a new hospital to comply with seismic retrofitting standards. When these plans were significantly changed, the determination was made to write off the accumulated costs which related to the previous hospital design. These costs written off totaled \$7,843,600 in 2008, and they are included in operating expenses.

NOTE 5 - LONG TERM OBLIGATIONS

Long-term obligations consist of the following at December 31, 2008 and 2007:

	2008	2007
ABAG Finance Authority for Nonprofit Corporations Hospital Revenue Certificates of Participation, \$60,100,000 fixed rate bonds series 2007; principal payable in annual installments ranging from \$1,085,000 in 2010 to \$31,065,000 in 2037; interest at state coupon rates ranging from 4.00% to 5.25%, payable semiannually.	\$ 60,100,000	\$ 60,100,000
ABAG Finance Authority for Nonprofit Corporations Hospital Revenue Certificates of Participation, \$30,000,000 fixed rate bonds Series 2005; principal payable in annual installments ranging from \$500,000 in 2010 to \$2,300,000 in 2034; interest at stated coupon rate of 6.15%, payable semiannually.	30,000,000	30,000,000
	<u>\$ 90,100,000</u>	<u>\$ 90,100,000</u>

The Series 2007 Certificates of Participation were issued during 2007 by the ABAG Finance Authority for Nonprofit Corporations. The 2007 Certificates of Participation were issued in a refinancing of the 1999 series Certificates of Participation. Children's agrees to make installment payments that, in aggregate, will be sufficient to pay all interest and principal on the Certificates of Participation as they become due. Under the terms of the loan and reimbursement agreements, Children's is subject to certain limitations on its ability to incur additional debt, to pledge assets as collateral, and to acquire or dispose of certain assets. Children's must also maintain certain financial ratios, including debt service coverage ratio and days cash on hand.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Plan's assets are invested in common stocks, corporate and government bonds, convertible securities, and money market funds.

The Children's uses a December 31 measurement date for its Plan. Changes in the benefit obligation and Plan assets for the Children's noncontributory defined benefit retirement plan are as follow:

	December 31,	
	2008	2007
Actuarial present value of benefit obligations:		
Benefit obligation at beginning of year	\$ 173,009,600	\$ 163,973,700
Service cost	12,282,300	11,314,600
Interest cost	11,193,900	9,727,700
Actuarial loss (gain)	(7,099,800)	(9,026,600)
Benefits paid	(3,580,000)	(2,979,800)
Benefit obligation at end of year	185,806,000	173,009,600
Change in Plan assets:		
Fair value of Plan assets at beginning of year	137,122,100	125,400,800
Actual return on Plan assets	(32,278,900)	6,751,200
Employer contributions	13,100,000	7,950,000
Benefits paid	(3,579,900)	(2,979,800)
Fair value of Plan assets at end of year	114,363,300	137,122,200
Funded status of the Plan	(71,442,700)	(35,887,400)
Unrecognized net actuarial loss (gain)	54,893,400	18,596,400
Unrecognized prior service cost	3,029,700	3,664,300
Accrued retirement benefit cost	\$ (13,519,600)	\$ (13,626,700)

The components of the Children's net periodic benefit cost associated with its noncontributory defined benefit retirement plan are as follow:

	Years Ended December 31,	
	2008	2007
Service cost	\$ 12,282,300	\$ 11,314,600
Interest cost	11,193,900	9,727,700
Expected return on Plan assets	(11,322,200)	(10,348,300)
Net loss recognition	204,200	654,000
Amortization of prior service cost	634,600	670,200
Net periodic benefit cost	\$ 12,992,800	\$ 12,018,200

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7 - RELATED ORGANIZATIONS

Children's receives support from Children's Hospital Branches, Inc. (the "Branches"). The accounts of the Branches are not consolidated with those of Children's, as described in Note 1. Summarized financial information of the Branches is not presented as it is not significant.

NOTE 8 - OPERATING LEASES

Children's has entered into operating lease arrangements for the lease of office space, facilities, vehicles, and equipment. The total amount of rental expense incurred during 2008 and 2007, under these operating leases was \$2,586,500 and \$2,313,300. Children's future minimum lease payments under non-cancelable operating leases with initial terms of one year or more consist of the following:

<u>Year Ending December 31,</u>	
2009	\$ 2,300,200
2010	1,613,200
2011	1,732,200
2012	1,528,000
2013	1,322,600
Thereafter	6,235,700
	<u>\$ 14,731,900</u>

NOTE 9 - COMMITMENTS AND CONTINGENCIES

The Children's receives grant funds for various programs. These funds may be subject to program compliance audits by the grantor and possible disallowance of expenditures. The Children's does not expect the amount of disallowance of expenditures, if any, to have a material adverse impact on the Children's financial position.

The Children's is aware of certain asserted and unasserted legal claims. While the outcome cannot be determined at this time, it is management's opinion that the liability, if any, from these actions will not have a material adverse effect on the Children's financial position.

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time. These laws and regulations include, but are not limited to, accreditation, licensure, government health care program participation requirements, reimbursement for patient services, and Medicare and Medi-Cal fraud and abuse. Government activity has continued with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs, together with the imposition of significant fines and penalties, as well as significant repayment for previously billed patient services. While the Children's is subject to similar regulatory reviews, there are no reviews currently underway and management believes that the outcome of any potential regulatory review will not have a material adverse effect on the Children's financial position.

Management believes that the Children's is in compliance with government law and regulations related to fraud and abuse and other applicable areas. While no material regulatory inquiries have been made other than discussed in Note 2, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

Children's is directly liable under an irrevocable letter of credit with a bank, totaling \$8.5 million and \$10.6 million at December 31, 2008 and 2007, which is required as security for the workers' compensation large dollar deductible arrangement as described in Note 1. No amounts were drawn on the letter of credit as of December 31, 2008 and 2007.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Accrued workers' compensation liability: The carrying amount reported in the balance sheet for accrued workers' compensation liability approximates its fair value.

Long-term obligations: Fair values of the Children's revenue notes are based on current traded value. The fair value of the Children's remaining long-term debt is estimated using discounted cash flow analyses, based on the Children's current incremental borrowing rates for similar types of borrowing arrangements.

Other long-term liabilities: The carrying amount reported in the balance sheet for other long-term liabilities approximates its fair value.

The carrying amounts and fair values of the Children's financial instruments at December 31, 2008 and 2007, are as follow:

	2008		2007	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Cash and cash equivalents	\$ 33,565,400	\$ 33,565,400	\$ 21,735,900	\$ 21,735,900
Investments, current portion	-	-	4,938,700	4,938,700
Assets limited as to use	7,383,700	7,383,700	20,906,000	20,906,000
Investments, less current portion	156,023,200	156,023,200	182,899,500	182,899,500
Accounts payable and accrued expenses	25,706,800	25,706,800	19,068,000	19,068,000
Accrued payroll and payroll related liabilities	30,485,900	30,485,900	29,680,600	29,680,600
Estimated third-party payor settlements payable	1,561,000	1,561,000	1,631,600	1,631,600
Accrued professional liability	3,416,000	3,416,000	3,250,500	3,250,500
Accrued workers' compensation liability	4,993,000	4,993,000	9,766,200	9,766,200
Long-term obligations	90,100,000	90,100,000	90,100,000	90,100,000
Other long-term liabilities	3,630,100	3,630,100	37,051,800	37,051,800

NOTE 12 - SUBSEQUENT EVENTS

Put Option - In 2005, CHRCF issued Merrill Lynch a put option on the 2005 revenue bonds, as described in Note 9. The put option was scheduled to expire June 1, 2009 if it was not exercised. On May 1, 2009, Merrill Lynch notified CHRCF that they were going to exercise the option effective June 1, 2009. CHRCF plans to sell \$21,500,000 of its Merganser bond investments, at a profit, and transfer that amount together with \$8,500,000 of unrestricted cash, in exchange for the exercised revenue bond guarantee.

Promissory Note - On April 9, 2009, Children's purchased a property for the operation of Children's Specialty Care Center Walnut Creek for a purchase price of \$14,750,000 and assumed a loan against the property in the amount of \$7,700,000.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended December 31, 2008

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA/ Contract Number	Federal Expenditures
Research and Development Cluster		
U.S. Department of Health and Human Services		
National Institutes of Health	Note 2	\$ 22,188,853
Food and Drug Administration	93.103	244,387
Centers for Disease Control and Prevention	93.283	184,365
Health Resources and Services Administration	Note 7	231,549
U.S. Department of Justice	Note 12	36,963
National Foundation of the Arts and the Humanities	45.301	44,174
U.S. Department of Agriculture	10.206	149,677
U.S. Department of Energy	81.UNKNOWN	158,684
Subtotal Direct Programs		<u>23,238,652</u>
Pass-Through Programs From:		
Bay Area Tumor Institute	93.399	106,062
Benaroya Research Institute at Virginia Mason	93.847	18,643
Children's Hospital and Regional Medical Center	93.103	58
Children's Hospital Research Foundation	93.859	9,397
Duke University	Note 11	51,138
DV Bio, Inc.	93.UNKNOWN	30,636
Fallbrook Engineering	93.061	137,115
GL Synthesis, Inc.	93.103	26,172
Lawrence Livermore National Laboratory	93.UNKNOWN	10,047
Lypro Bioscience	93.838	218,348
March of Dimes	Note 5	141,471
Massachusetts General Hospital	93.853	156,328
New England Research Institute	93.839	115,287
Point Vista Software	93.307	61,740
Public Health Foundation Enterprises, Inc.	93.283	31,487
Science Applications International Corporation	Note 6	59,533
The George Washington University	93.847	32,597
The Regents of the University of California, Berkeley	Note 10	18,466
The Regents of the University of California, Davis	Note 4	530,310
The Regents of the University of California, San Francisco	Note 3	832,842
The Regents of the University of Minnesota	Note 9	274,257
The University of North Carolina at Chapel Hill	93.213	111,398
University of South Florida	93.847	190,317
Wake Forest University Health Sciences	93.847	442,250
Subtotal Pass-Through Programs		<u>3,605,899</u>
Total Research and Development Cluster		<u>26,844,551</u>

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended December 31, 2008

NOTE 1A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting - The accompanying schedule of expenditures of federal awards includes the federal grant activity of Children's Hospital & Research Center at Oakland (the "CHRCO") and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts may differ from accounts presented in, or used in the preparation of, the consolidated financial statements.

Federal Expenditures - Federal expenditures of \$34,058,142 are included in CHRCO's consolidated financial statements as "research and specific purpose grant expenses."

NOTE 1B - SUBRECIPIENTS

Certain funds are passed through to subrecipient organizations by CHRCO. Expenditures incurred by the subrecipients and reimbursed by CHRCO are included in the schedule of expenditures of federal awards. CHRCO is also the subrecipient of federal funds, which are reported as expenditures and listed separately as federal pass-through funds. Of the federal expenditures presented in the schedule of expenditures of federal awards, CHRCO provided federal awards to subrecipients as follows:

Federal CFDA Number	Program Title	Amount Provided to Subrecipients
93.110	Maternal and Child Health Federal Consolidated Program	\$ 13,500
93.153	Coordinated Services and Access to Research for Women, Infants, Children and Youth	1,155,622
93.172	Human Genome Research	4,407,851
93.375	Biomedical Research and Research Training	20,000
93.393	Cancer Cause and Prevention Research	155,877
93.396	Cancer Biology Research	27,046
93.837	Heart and Vascular Diseases Research	1,367,202
93.838	Lung Diseases Research	153,710
93.839	Blood Diseases and Resources Research	305,905
93.847	Diabetes, Endocrinology and Metabolism Research	61,329
93.849	Kidney Diseases, Urology and Hematology Research	5,971
93.855	Allergy, Immunology and Transplantation Research	290,211
93.865	Child Health and Human Development Extramural Research	83,504
93.866	Aging Research	34,409
93.914	HIV Emergency Relief Project Grants	8,738
93.UNKNOWN	Respiratory Distress in Newborns and Its Relationship to Group B Streptococcal Colonization (part of the R&D Cluster)	10,000
93.UNKNOWN	Bioessays Project (part of the R&D Cluster)	40,000

NOTE 2 - NATIONAL INSTITUTES OF HEALTH

Federal CFDA and agency or pass-through numbers are as follow:

	Federal CFDA Number	Agency or Pass-Through Number	Federal Expenditure
Research and Development Cluster	93.113	1R21ES016581-01	\$ 24,964
	93.113	5 R21 ES013845-02	57,628
	93.121	5 R21 DE017005-02	2,557

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended December 31, 2008

Federal CFDA Number	Agency or Pass-Through Number	Federal Expenditure
93.859	5 R01 GM066954-04	31,607
93.859	5 R01 GM069717-02	307,742
93.865	1 R01 HD046741-04	480,030
93.865	5 R01 HD053036-03	264,586
93.866	5 R21 AG025944-02	40,185
93.866	5 R21 EY016101-02	34,086
93.989	1 R03 TW007754-01	40,491
93.UNKNOWN	HHSN267200700011C	727,180
93.UNKNOWN	HHSN268200617186C	313,734
		<u>\$ 22,188,853</u>

NOTE 3 - UNIVERSITY OF CALIFORNIA, SAN FRANCISCO

Federal CFDA and agency or pass-through numbers are as follow:

	Federal CFDA Number	Agency or Pass-Through Number	Federal Expenditure
Research and Development Cluster	93.361	5 R21 NR010600-02	\$ 6,781
	93.389	5 KL RR024130-03	13,418
	93.389	5 UL1 RR024131-03	737,284
	93.846	P01 AR050440	75,359
			<u>\$ 832,842</u>

NOTE 4 - UNIVERSITY OF CALIFORNIA, DAVIS

Federal CFDA and agency or pass-through numbers are as follow:

	Federal CFDA Number	Agency or Pass-Through Number	Federal Expenditure
Research and Development Cluster	93.172	3 R01 HG002942-04	\$ 6,073
	93.375	1 P60 MD000222-07	178,415
	93.375	1 P60 MD000222-04	12,365
	93.375	P60 MD000222	89,875
	93.389	1 U42 RR024244-02	243,582
			<u>\$ 530,310</u>

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended December 31, 2008

NOTE 8 - ALAMEDA COUNTY

Federal CFDA and agency or pass-through numbers are as follow:

	Federal CFDA Number	Agency or Pass-Through Number	Federal Expenditure
Other	14.UNKNOWN	Contract No. CMDEV 2029	\$ 11,758
	93.645	Master Contract 900159 Procurement # 2162	29,239
	93.658	Master Contract 900159 Procurement # 2273	4,263
	93.658	Master Contract 900159 Procurement # 2459	7,818
	93.778	FSS2007-09-05	318,411
	93.914	PHG01HA60200	123,729
			<u>\$ 495,218</u>

NOTE 9 - UNIVERSITY OF MINNESOTA

Federal CFDA and agency or pass-through numbers are as follow:

	Federal CFDA Number	Agency or Pass-Through Number	Federal Expenditure
Research and Development Cluster	93.393	5 R01 CA11135-03	\$ 27,218
	93.395	5 P01 CA111412-04	247,039
			<u>\$ 274,257</u>

NOTE 10 - UNIVERSITY OF CALIFORNIA, BERKELEY

Federal CFDA and agency or pass-through numbers are as follow:

	Federal CFDA Number	Agency or Pass-Through Number	Federal Expenditure
Research and Development Cluster	93.113	5 R01 ES009137-10	\$ 4,233
	93.837	1 R01 HL072110	14,233
			<u>\$ 18,466</u>

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended December 31, 2008

The following information is provided as requested under the State of California, Office of Emergency Services' Recipient Handbook, §8215. Expenditure amounts per State of California Report of Expenditures and Request for Funds amounts were obtained from monthly reports submitted to the Office of Emergency Services.

	Federal CFDA Number	Hospital Match	Federal Funds
Grant numbers: AT07 03 1500; AT08 04 1500			
Grant periods: 10/01/07 to 09/30/08 and 10/01/08 to 09/30/09			
Audit period: 01/01/08 to 12/31/08			
Amount per State of California Report of Expenditures and Request for Funds			
Child Abuse Treatment Program			
Personal services		\$ 46,251	\$ 184,995
Operating expenses		504	2,014
		<u>\$ 46,755</u>	<u>187,009</u>
Amount per Schedule of Expenditures of			
Federal Awards	16.575		<u>196,806</u>
Difference			<u>\$ (9,797)</u>
Revenue received from State			<u>\$ 175,655</u>

The difference is due to timing differences between actual expenditure of funds and State reporting thereto.

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND
OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH *GOVERNMENT AUDITING STANDARDS*

Board of Directors
Children's Hospital & Research Center at Oakland

We have audited the consolidated financial statements of Children's Hospital & Research Center at Oakland (the "CHRCO") as of and for the year ended December 31, 2008, and have issued our report thereon dated May 28, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered CHRCO's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of CHRCO's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of CHRCO's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be significant deficiencies in internal control over financial reporting; such items are listed as findings 2008-01 and 2008-02.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the consolidated financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider item 2008-02 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether CHRCO's consolidated financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of consolidated financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

CHRCO's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit CHRCO's response and, accordingly, we express no opinion on it.

**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

Board of Directors
Children's Hospital & Research Center at Oakland

Compliance

We have audited the compliance of Children's Hospital & Research Center at Oakland (the "CHRCO") with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133, *Compliance Supplement*, that are applicable to its major federal programs for the year ended December 31, 2008. CHRCO's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal programs is the responsibility of CHRCO's management. Our responsibility is to express an opinion on the CHRCO's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about CHRCO's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on CHRCO's compliance with those requirements.

In our opinion, CHRCO complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs for the year ended December 31, 2008.

Internal Control over Compliance

The management of CHRCO is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered CHRCO's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of CHRCO's internal control over compliance.

A *control deficiency* in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a Federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year Ended December 31, 2008

SECTION I – SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

- Material weakness(es) identified? ☒ yes ☐ no
- Significant deficiency(ies) identified that are not considered to be material weaknesses? ☒ yes ☐ none reported

Noncompliance material to financial statements noted? ☐ yes ☒ no

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? ☐ yes ☒ no
- Significant deficiency(ies) identified that are not considered to be material weakness(es)? ☐ yes ☒ none reported

Type of auditor's report issued on compliance for major program: Unqualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133? ☐ yes ☒ no

Identification of major programs

CFDA Number(s)

*Various
93.153*

Name of Federal Program or Cluster

*Research and Development Cluster
Coordinated Services and Access to Research for Women, Infants,
Children and Youth*

Dollar threshold used to distinguish between Type A and Type B programs

\$ 1,021,744

Auditee qualified as low-risk auditee?

☒ yes ☐ no

CHILDREN'S HOSPITAL & RESEARCH CENTER AT OAKLAND
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year Ended December 31, 2008

Finding 2008-02 – Schedule of Expenditures of Federal Awards – Material Weakness

Criteria – OMB Circular A-133 section .300 states that “The auditee shall (a) Identify, in its accounts, all Federal awards received and expended and the Federal programs under which they were received. Federal program and award identification shall include, as applicable, the CFDA title and number, award number and year, name of Federal agency, and name of the pass-through entity.” And “(d) Prepare appropriate financial statements, including the schedule of expenditures of federal awards in accordance with (OMB Circular A-133 section) .310.” Section .310 states: “(a) Financial statements. The auditee shall prepare financial statements that reflect its financial position, results of operations or changes in net assets, and, where appropriate, cash flows for the fiscal year audited. The financial statements shall be for the same organizational unit and fiscal year that is chosen to meet the requirements of this part. However, organization-wide financial statements may also include departments, agencies, and other organizational units that have separate audits in accordance with §.500(a) and prepare separate financial statements. (b) Schedule of expenditures of Federal awards. The auditee shall also prepare a schedule of expenditures of Federal awards for the period covered by the auditee's financial statements.

Condition – The Alameda County EPSDT program was initially included within the 2008 schedule of expenditure of federal awards (SEFA) yet this program is not subject to OMB circular A-133 because it does not meet the definition of a federal expenditure subject to OMB A-133.

Context – The expenditures initially listed in the SEFA totaled \$7,957,322.

Effect – Management prepared an inaccurate schedule of expenditures of federal awards.

Cause – The pass-through funding agency was unable to provide supporting documentation in a timely manner related to changes in funding.

Recommendation – We recommend that entity obtain timely and clear supporting source documentation for awards received if not evident within the award itself.

Management's Response –The EPSDT program had been included in the A133 audit due to the language in the contract with the County directing the Hospital to include this as part of the oversight. Until this year, the source of funding for determination of inclusion or exclusion from the SEFA list was miss-identified as CFDA number 93.658 Foster Care Title IV-E. During the audit, hospital staff verified with the County the source of funding was exclusively Medi-Cal Fee for Service, and therefore not appropriate for inclusion on the SEFA. A corrected SEFA was issued mid-audit.

Management is developing a process to have an annual confirmation with the County regarding programs that meet A133 requirement to ensure an accurate SEFA list is provided at the beginning of the audit process. In addition the SEFA list will not be released without full review of by management.

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

None noted.